

Message Text

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ACTION ARA-10

INFO OCT-01 EUR-12 NEA-10 IO-13 ISO-00 AGRE-00 PA-02 PRS-01
XMB-04 FEA-01 ERDA-07 AID-05 CEA-01 CIAE-00 CIEP-02
COME-00 DODE-00 EB-07 FPC-01 H-02 INR-07 INT-05 L-03
NSAE-00 NSC-05 OMB-01 PM-04 USIA-15 OES-06 SP-02
SS-15 STR-04 TRSE-00 ACDA-10 /156 W
-----292004Z 023596 /50 43

R 291625Z DEC 76
FM AMEMBASSY BRASILIA
TO SECSTATE WASHDC 9338
INFO USMISSION OECD PARIS
USDEL MTN GENEVA
USMISSION GENEVA
AMEMBASSY TEHRAN
AMEMBASSY JIDDA
AMCONSUL RIO DE JANEIRO
AMCONSUL SAO PAULO
AMEMBASSY CARACAS
US EC MISSION BRUSSELS 0242
USUN NEW YORK 0643

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DEPARTMENT PASS BAGHDAD

E.O. 11652: N/A
TAGS: ENRG, ETRD, EAGR, BR
SUBJECT: PETROLEUM DEVELOPMENTS-BRAZIL AT YEAREND

REF: (A) RIO DE JANEIRO A-93, CERP 0425 (B) BRASILIA 10288
(C) BRASILIA 10420

FOLLOWING MESSAGE WAS PREPARED BY MINERAL OFFICER, RIO AND
EMBASSY ECON STAFF.

1. SUMMARY. BRAZIL CONTINUES TO WRESTLE WITH THE PERSISTENT
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PROBLEMS OF SLOWLY DECLINING OIL PRODUCTION, STEADILY IN-
CREASING CONSUMPTION OF SEVERAL KEY PETROLEUM DERIVATIVES,
ESPECIALLY DIESEL OIL AND FUEL OIL (BUT NOT GASOLINE), AND AN
EVER INCREASING IMPORT BILL FOR FOREIGN CRUDE. IN RECENT YEARS
BRAZIL HAS STEPPED UP SHARPLY ITS PETROLEUM IMPORTS FROM IRAQ,
KUWAIT AND IRAN, COUNTRIES WITH WHICH BRAZIL HAS MADE SPECIAL EFFORTS

TO PROMOTE TWO-WAY ECONOMIC INTERCHANGE. BRAZIL HAS SIGNED THE FIRST TWO OF AN EXPECTED SERIES OF "RISK" (I.E. SERVICE) CONTRACTS FOR OIL EXPLORATION IN OFFSHORE AREAS. BUT SOME POTENTIAL FOREIGN CONTRACTORS STILL BELIEVE PETROBRAS IS TRYING TO DRIVE TOO HARD A BARGAIN. PROSPECTS REMAIN SLIM, IN THE EMBASSY'S JUDGEMENT, THAT BRAZIL CAN REDUCE SIGNIFICANTLY SHARE OF IMPORTED (VERSUS DOMESTIC) PETROLEUM UNTIL AT LEAST THE EARLY 1980'S. END SUMMARY.

2. PRODUCTION: FOR THE FIRST 10 MONTHS OF 1976, BRAZILIAN OIL PRODUCTION WAS DOWN BY 2.52 PERCENT COMPARED WITH THE SAME PERIOD IN 1975. AVERAGE OUTPUT FELL FROM 172,082 BARRELS PER DAY (BPD) (JAN.-OCT. 1975) TO 167,130 BPD (JAN. OCT. 1976). THE DECLINE WAS DUE PRINCIPALLY TO A DROP IN PRODUCTION FROM ONSHORE FIELDS IN BAHIA (DOWN BY ABOUT 9 PERCENT) WHICH WAS COMPENSATED FOR ONLY PARTIALLY BY AN INCREASE FROM OFFSHORE WELLS (UP BY 18.2 PERCENT). BRAZIL'S SLOW BUT STEADY PRODUCTION DECLINE STARTED IN 1975 (PRODUCTION IN 1975 WAS 177,300 BPD, VERSUS 182,100 BPD IN 1974) AND HAS CONTINUED TO THE PRESENT. THIS TREND FOLLOWED A LEVELING OFF IN PRODUCTION BETWEEN 1969 AND 1974, WHEN PRODUCTION GREW BY AN AVERAGE OF 0.76 PERCENT PER YEAR. FROM 1964 TO 1969, BY CONTRAST, PRODUCTION CLIMBED BY AN AVERAGE OF 13.9 PERCENT PER YEAR.

3. CONSUMPTION. APPARENT CONSUMPTION (REAL CONSUMPTION PLUS INVENTORY ACCUMULATION BY BUYERS) OF PETROLEUM DERIVATIVES IN THE FIRST ELEVEN MONTHS OF 1976 (AN AVERAGE OF UNCLASSIFIED

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860,000 BPD) WAS UP BY 8.6 PERCENT OVER THE SAME PERIOD IN 1975 (788,000 BPD ON AVERAGE). DIESEL OIL AND FUEL OIL ACCOUNTED FOR 86 PERCENT OF THE INCREASE, CONTRASTED AGAINST THE 3 PERCENT CONTRIBUTION OF REGULAR GASOLINE. REFLECTING THIS PATTERN OF INCREASES, MINES AND ENERGY MINISTER UEKI HAS SAID, ACCORDING TO A PRESS REPORT, THAT THE REAL PRICE OF DIESEL OIL AND FUEL OIL WOULD BE RAISED (GASOLINE PRICES HAVE BEEN RAISED BY MORE THAN PRICES FOR DIESEL AND FUEL OIL). STATISTICS ON APPARENT CONSUMPTION FOR SEVERAL CATEGORIES OF PETROLEUM DERIVATIVES ARE:

	JANUARY-NOVEMBER			
	1975	1976		PERCENT CHANGE
	(BARRELS PER DAY)			
FUEL OIL	230,300	267,000		11.6
DIESEL OIL	184,700	217,000		17.5
REGULAR GASOLINE	225,300	227,400		0.9
AVIATION KEROSENE	27,900	27,300		-2.0

OTHERS 119,800 127,800 6.6

4. IMPORTS: BRAZIL'S IMPORTS OF CRUDE PETROLEUM IN THE FIRST THREE QUARTERS OF 1976 AMOUNTED TO 204.1 MILLION BARRELS, AT A COST OF 2.568 BILLION DOLLARS (FOB) ACCORDING TO PETROBRAS STATISTICS. BRAZIL ALSO IMPORTS MODEST AMOUNTS OF REFINED PRODUCTS. THE EMBASSY PROJECTS THAT TOTAL IMPORTS OF ALL PETROLEUM PRODUCTS IN 1976 WILL BE ON THE ORDER OF \$3.6-3.8 BILLION DOLLARS, UP BY ABOUT 17-24 PERCENT FROM 1975 IMPORTS OF \$3.07 BILLION. STATISTICS ON THE SHARE OF BRAZIL'S CRUDE PETROLEUM IMPORTS BY COUNTRY-OF-ORIGIN FOR 1974, 1975 AND THE FIRST THREE QUARTERS OF 1976 ARE (SOURCE: PETROBRAS):

COUNTRY	'74	'75	JAN:SEPT. '76
(FIGURES ARE PERCENTAGES OF TOTAL IMPORTS)			
IRAQ	22.8	29.4	31.0
SAUDI ARABIA	46.8	32.4	23.3
KUWAIT	2.8	10.6	11.7

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IRAN	1.4	5.4	10.8
NEUTRAL ZONE	4.6	3.2	5.0
LIBYA	10.1	6.6	4.6
UAE	0.8	2.4	2.6
ALGERIA	2.8	2.5	1.5
VENEZUELA	2.7	1.7	1.4
OTHER	5.4	5.6	9.1
TOTAL	100	100	100

NOTE BY OC/T: NOT PASSED BAGHDAD.

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5. THESE STATISTICS REVEAL TWO INTERESTING TRENDS:

(A) BRAZIL HAS SHARPLY INCREASED ITS PETROLEUM IMPORTS FROM SAUDI ARABIA, AND INCREASED ITS IMPORTS FROM IRAQ, KUWAIT AND IRAN, THREE COUNTRIES WITH WHICH BRAZIL HAS MADE SPECIAL EFFORTS TO ACHIEVE TWO-WAY ECONOMIC INTERCHANGE. BRAZILIAN EXPORTS TO IRAQ CLIMBED FROM 38.1 MILLION DOLLARS IN 1974 TO 178.7 MILLION DOLLARS IN 1975. ALSO, A PETROBRAS SUBSIDIARY HAS BEEN EXPLORING FOR OIL IN IRAQ. REGARDING KUWAIT, BRAZILIAN EXPORTS STILL ARE RELATIVELY LOW BUT RISING (THEY WERE 1.4 MILLION DOLLARS IN 1974, AND 15.6 MILLION DOLLARS IN 1976). KUWAIT ALSO HAS ESTABLISHED A MODEST INVESTMENT FUND FOR UNCLASSIFIED

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BRAZILIAN PROJECTS. TURNING TO IRAN, BRAZILIAN EXPORTS TO THAT COUNTRY CLIMBED FROM 55.4 MILLION DOLLARS IN 1973 TO 76.0 MILLION DOLLARS IN 1976. THIS TREND DOES NOT, HOWEVER, REVEAL THE FULL RANGE OF THE EXPANSION OF BRAZILIAN-IRANIAN COOPERATION NOW UNDERWAY (REF.B).

(B) BRAZIL HAS DIVERSIFIED ITS SOURCES OF SUPPLY-- IN 1974 THE LARGEST SUPPLIER ACCOUNTED FOR 46.8 PERCENT OF IMPORTS; IN 1976 (JAN.-SEPT.), THE LARGEST SUPPLIER ACCOUNTED FOR ONLY 31.0 PERCENT BRAZIL'S TOP FIVE SUPPLIERS ACCOUNTED FOR 86.9 PERCENT OF IMPORTS IN 1974, VERSUS 81.9 PERCENT IN JAN.-SEPT. 1976.

6. DOMESTIC PRODUCTION OF CRUDE (IN TONS) AS A FRACTION OF IMPORTS PLUS DOMESTIC PRODUCTION HAS FALLEN STEADILY OVER THE PAST DECADE--FROM 40.0 PERCENT IN 1967 TO 19.7 PERCENT IN 1975.

7. ALCOHOL-FOR-GASOLINE SUBSTITUTION: THE GEISEL ADMINIS-

TRATION'S PROGRAM TO SPUR DIRECT DISTILLATION OF ALCOHOL FROM SUGAR CANE AND MANIOC IN ORDER TO MIX IT WITH GASOLINE (UP TO 20 PERCENT) GOT OFF TO A SLUGGISH START THIS YEAR. (ANHYDROUS ALCOHOL, MOST OF WHICH IS PRODUCED AS A BY-PRODUCT OF SUGAR CANE DISTILLATION INTO REFINED SUGAR, NOW CONSTITUTES LESS THAN THREE PERCENT OF RETAIL GASOLINE.) THE NATIONAL ALCOHOL COUNCIL HAS APPROVED 83 PROJECTS BUT FINANCING HAS BEEN MADE AVAILABLE FOR ONLY A FRACTION OF THESE. (THE BANK OF BRAZIL HAS APPROVED \$144 MILLION IN FINANCING FOR PROJECTS.)

UNDER THE NATIONAL ALCOHOL PROGRAM, THE NATIONAL PETROLEUM COUNCIL IS PLEDGED TO PURCHASE ALL ALCOHOL DISTILLED, AT A GUARANTEED PRICE THAT PRESUMABLY WOULD BE AS HIGH AS WHAT THE DISTILLERIES COULD GET IF THEY PRODUCED REFINED SUGAR INSTEAD OF ALCOHOL. THIS PRICE PROBABLY WOULD EXCEED THE INTERNATIONAL PRICE FOR ALCOHOL. THE GOB WOULD RESELL THE ALCOHOL TO DOMESTIC REFINERIES

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(I.E., PETROBRAS) AT A PRICE ABOVE ITS PURCHASE PRICE, BUT SALES TO THE CHEMICAL INDUSTRY WOULD BE SUBSIDIZED. DESPITE THE QUESTIONABLE ECONOMICS OF THE ALCOHOL PROGRAM, AND ITS SLOW START, GOB LEADERS RECENTLY REAFFIRMED THEIR COMMITMENT TO THE PROGRAM.

8. RISK CONTRACTS: CONTRARY TO EXPECTATIONS, PETROBRAS MOVED SLOWLY THIS YEAR IN IMPLEMENTING PRESIDENT GEISEL'S DECISION, ANNOUNCED IN OCTOBER 1975, TO PERMIT FOREIGN COMPANIES TO EXPLORE FOR OIL THROUGH RISK (SERVICE) CONTRACTS. FOLLOWING AN INITIAL SHOW OF INTEREST BY 40 FOREIGN PETROLEUM COMPANIES, ONLY FIVE RESPONDED TO PETROBRAS' INVITATION TO NEGOTIATE CONTRACTS. TO DATE, PETROBRAS HAS SIGNED CONTRACTS WITH A SUBSIDIARY OF BP FOR AN AREA IN THE SANTOS BASIN, AND WITH A SUBSIDIARY OF SHELL FOR AN AREA IN THE FOZ DO AMAZONAS-AMAPA BASIN. IN ADDITION, PETROBRAS HAS SIGNED A "BASIC DOCUMENT" WITH ELF-AGIP, WHICH WILL BE FOLLOWED BY SIGNATURE OF A FORLAL CONTRACT WITH THE SUBSIDIARY OF ELF-AGIP THAT WILL DO THE EXPLORATION IN BRAZIL. THIS LEAVES

NEGOTIATIONS WITH TEXACO AND EXXON, BOTH OF WHICH HAVE MARKETING OPERATIONS IN BRAZIL. PETROBRAS HAS EXPRESSED ITS HOPE TO HAVE CONTRACTS WITH THESE COMPANIES SIGNED BY MID-JANUARY 1977.

9. THE RELUCTANCE OF MANY COMPANIES TO NEGOTIATE CONTRACTS MAY BE RELATED TO AN UNWILLINGNESS BY PETROBRAS TO OFFER SUFFICIENTLY ATTRACTIVE TERMS AND AREAS FOR EXPLORATION. MANY INDUSTRY SOURCES TEND TO AGREE WITH CRITICISMS MADE IN EARLY OCTOBER "WALL STREET JOURNAL"

ARTICLE, WHICH REFERRED TO "UNREALISTIC, HARSH" TERMS IN THE RISK CONTRACTS AND TO AN "ANTAGONISTIC" ATTITUDE WITHIN PETROBRAS TOWARD FOREIGN COMPANY BIDDERS.

10. THE SYSTEM OF TEMPORARY PLATFORMS IN THE CAMPOS BASIN--
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WHICH THE GOB HAD HOPED WOULD PRODUCE ABOUT 50,000 BPD BY END OF 1977--HAS RUN INTO DIFFICULTIES, APPARENTLY RELATED TO INSUFFICIENT FLOW FROM SOME OF THE WELLS. CAMPOS PRODUCTION, THEREFORE, WILL BE DEALYED. PETROBRAS HAS NOT COMMITTED ITSELF TO A NEW TARGET DATE FOR FULL PRODUCTION RATES IN CAMPOS. THIS ALSO IMPLIES, AT A MINIMUM, SLIPPAGE IN THE EARLIER TARGET OF 200,000 BPD FROM THE BASIN BY 1980-81. FURTHERMORE, THE TENTATIVE RESERVE ESTIMATES FOR THE BASIN HAVE BEEN VERY SUBSTANTIALY REDUCED.

11. COMMENT: BRAZIL HAS ONLY SLIM PROSPECTS FOR REDUCING SIGNIFICANTLY ITS DEPENDENCE ON IMPORTED PETROLEUM PRIOR TO THE EARLY 1980'S, IF THEN. CONSUMPTION OVER THE NEXT FIVE YEARS PROBABLY WILL INCREASE. AND IT IS UNCLEAR THAT THE SUM OF (A) EXPANDED OFFSHORE PRODUCTION LESS DECLINES IN ONSHORE PRODUCTION, (B) POSSIBLE INCREMENTAL ALCOHOL SUBSTITUTION FOR GASOLINE, AND (C) INCREMENTAL REDUCTIONS IN CONSUMPTION FOR SOME USES DUE TO CONSERVATION MEASURES, WILL OFFSET THE INCREASED DEMAND FOR PETROLEUM PRODUCTS ARISING FROM ECONOMIC GROWTH. ONE HOPEFUL SIGN IS THAT RECENT ECONOMIC PERFORMANCE SUGGESTS THAT ECONOMIC GROWTH IN BRAZIL IS BECOMING RELATIVELY LESS ENERGY-INTENSIVE OVER TIME. OVER THE SIX-YEAR PERIOD 1970-1975, GROSS DOMESTIC PRODUCT EXPANDED IN REAL TERMS BY 70.9 PERCENT, THE CONSUMPTION OF PETROLEUM DERIVATIVES (IN CRUDE OIL EQUIVALENTS, COE) INCREASED BY 57.8 PERCENT, AND TOTAL PRIMARY ENERGY CONSUMPTION (IN COE'S) FROM ALL SOURCES CLIMBED BY ONLY 44.8 PERCENT. THEREFORE, OVER THIS PERIOD, THE ELASTICITY OF ECONOMIC GROWTH WITH RESPECT TO THE CONSUMPTION OF PETROLEUM DERIVATES WAS 1.23; AND THE ELASTICITY WITH RESPECT TO TOTAL PRIMARY ENERGY CONSUMPTION WAS EVEN HIGHER, 1.58.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: PETROLEUM INDUSTRY, IMPORTS, PRODUCTION DATA
Control Number: n/a
Copy: SINGLE
Draft Date: 29 DEC 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Authority: n/a
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 JAN 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976BRASIL10590
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D760475-0431
From: BRASILIA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t1976125/aaaaadv.tel
Line Count: 332
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION ARA
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 7
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: 77 RIO DE JANEIRO A-93, 77 BRASILIA 10288, 77 BRASILIA 10420
Review Action: RELEASED, APPROVED
Review Authority: vogelfj
Review Comment: n/a
Review Content Flags:
Review Date: 07 JUN 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <07 JUN 2004 by chengls>; APPROVED <27 DEC 2004 by vogelfj>; APPROVED <27 DEC 2004 by vogelfj>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: PETROLEUM DEVELOPMENTS-BRAZIL AT YEAREND
TAGS: ENRG, ETRD, EAGR, BR
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006